

Supreme Court, U.S.
FILED

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No. 79-264

IN THE SUPREME COURT OF THE UNITED STATES

MICHAEL RODAK, JR., CLERK

October Term, 1979

WALLACE W. WATKINS, Petitioner,

v.

UNITED STATES OF AMERICA, Respondent

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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August 14, 1979

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 PETITION FOR A WRIT OF CERTIORARI
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Petitioner, Wallace W. Watkins,
 prays that a writ of certiorari issue to
 review the opinion and judgment of the
 United States Court of Appeals for the
 Ninth Circuit entered on June 13, 1979,
 which affirmed the order of the United
 States District Court for the District of
 Oregon.

OPINION BELOW

The opinion of the Court of Appeals
 is not yet officially reported. It is at-
 tached as Appendix A, infra. The petition

for rehearing and suggestion for rehearing in banc was denied July 27, 1979 (see Appendix B, infra).

JURISDICTION

The jurisdiction of this Court is invoked under 28 U.S.C. § 1254.

QUESTION PRESENTED

Whether, in a trial for income tax evasion, the government should be permitted to introduce evidence of failure to file tax returns in pre-prosecution years where no evidence of a duty to file is produced?

STATEMENT OF THE CASE

Petitioner was convicted on three counts of willfully attempting to evade his income taxes for the period 1971 through 1973. 26 U.S.C. § 7201. He urged three grounds for reversal of his conviction, each of which was rejected by the Ninth Circuit in its opinion affirming the conviction. A single ground for certiorari is presented here with the following facts

being pertinent.

At the trial, the government was initially permitted to show, over repeated defense objection, that the defendant failed to file federal income tax returns during the years 1958 through 1970, a thirteen year period preceding the indictment years. Before submitting the case to the jury, the trial judge struck evidence relating to defendant's failure to file federal returns prior to 1968, and admitted evidence of prior failures to file for 1968-1970 on the element of intent. On appeal, the defendant argued that admission of the prior failures to file was permissible only if the government proved that the defendant had a duty to file returns for those years. This argument was rejected by the Ninth Circuit on the grounds that its previous decision in United States v. Snow, 529 F.2d 224 (C.A.9, 1976) permits proof of prior failures to file on the element of

intent whether or not a duty to file has been shown.

REASONS FOR GRANTING THE WRIT

Defendant's request for certiorari is based on the fundamental proposition that prior failures to file tax returns (a misdemeanor under 26 U.S.C. § 7203 if willful) simply is not relevant in a felony prosecution for tax evasion¹ unless the government first shows that the defendant had a duty to file returns in those earlier years, i.e. that the prior failure to file was illegal or wrongful.

The Internal Revenue Code, and appropriate regulations, make it clear that only individuals having the requisite amount of gross income are required to file

1. The government's theory at trial was that, in addition to failing to file his tax returns for the prosecution years (a misdemeanor), defendant had also attempted to evade tax (a felony) by concealing his financial affairs from the Internal Revenue Service.

income tax returns. 26 U.S.C. § 6012, Treasury Regulations § 1.6012-1. For the years in question in this case (1968 through 1970, the pre-prosecution period) the government was required to show that the defendant received \$600 or more of gross income before being required to file a return for any year. The government produced no such proof in this case.

We have found no case discussing the issue of whether the government must prove a duty to file tax returns before permitting proof of earlier failures to file on the element of intent during the prosecution period. The decisions holding that a prior or subsequent failure to file is admissible on the element of willfulness in either a tax evasion or failure to file case contain no discussion of this issue.² Nor have we been able to find

2. See, e.g., Ayash v. United States, 35 F.2d 1009 (10th Cir., 1968); United (Cont.)

any case in which the point was expressly raised as here. To our knowledge, then, the Ninth Circuit's specific holding that a duty to file is not required before such proof is allowed is unprecedented.

The court's holding wrongly interprets Rule 404(b) Federal Rules of Evidence, which admits proof of prior similar acts only if the such acts are criminal or wrongful. See, for example, United States v. Brashier, 548 F.2d 1315, 1325, (C.A.9 1976). Surely a failure to file a tax return without proving an accompanying duty to file is obviously not a "crime" or "wrong" admissible for any purpose within the meaning of Rule 404(b). Moreover, the Court's holding also results in shifting

2. (Cont.) States v. Magnus, 365 F.2d 1007 (2d Cir.), cert. denied, 386 U.S. 909 (1966); United States v. Ming, 466 F.2d 1000 (7th Cir.), cert. denied, 409 U.S. 915 (1972); United States v. Farris, 517 F.2d 226 (7th Cir.), cert. denied, 423 U.S. 892 (1975); United States v. Snow, 529 F.2d 224, 226 (9th Cir.), cert. denied, 429 U.S. 821 (1976).

the burden of proof to the defendant to establish a legal reason for him not to file a return in the year involved, i.e. that he did not make sufficient gross income to require a filing, that he was hospitalized or otherwise incapacitated at the time of the required filing, or the like. We believe that the Solicitor General will acknowledge that the course of conduct that was followed in this case by the prosecution, viz: proving a mere failure to file without an accompanying duty to do so -- is not in accordance with Department of Justice policy or instructions. The government's practice of utilizing prior or subsequent failures to file in a tax evasion or failure to file the case is widespread. See, e.g., cases cited in f.n. 2. Now that such a rule has been sanctioned by the court below it may be expected that government prosecutors will forego the more stringent (and we submit legally correct) requirement of proving

a duty to file. This Court should grant certiorari to resolve the important issue presented.

CONCLUSION

For the reasons stated, this writ should be granted and the judgment of the Court of Appeals for the Ninth Circuit should be reversed.

Respectfully submitted,

NORMAN SEPENUK

By Norm Sep
Norman Sepenuk
Attorney for Petitioner

APPENDIX A
A-1

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,)
)
 Plaintiff-Appellee,) No. 78-2733
)
 v.) OPINION
)
 WALLACE W. WATKINS,)
)
 Defendant-Appellant.)

Appeal from the United States
District Court of Oregon

Before: KILKENNY and SNEED, Circuit
Judges, and WATERS,* District
Judge.

Watkins appeals from his conviction
after jury trial on three counts of tax
evasion, 26 U.S.C. § 7201. He attacks the
district court's admission of three types
of evidence. Our jurisdiction is based on
28 U.S.C. § 1291. We affirm.

I.

Procedural History.

Appellant Watkins was indicted June

*Hon. Laughlin E. Waters, United States
District Court Judge for the Central Dis-
trict of California, sitting by designa-
tion.

29, 1977 on five counts. Three counts alleged that he willfully attempted to evade taxes for the years 1971 through 1973; two counts charged Watkins and others with stealing, and conspiring to steal, timber owned by the United States. The trial court ordered separate trials for the timber theft counts and the tax evasion counts. The theft charges were tried first and a mistrial declared after the jury was unable to reach a verdict. Thereafter the tax evasion counts were tried, and the jury convicted Watkins on each of three counts of attempted tax evasion. The trial judge sentenced Watkins to two and one-half years' imprisonment and imposed a \$5,000 fine.

II.

Alleged Errors of Trial Court.

Appellant in this appeal urges that his convictions should be reversed because the trial court erred in three respects.

Concisely put, these alleged errors are as follows:

- I. The trial judge erred in admitting evidence of theft in the trial for tax evasion,
- II. The trial judge erred in admitting into evidence declarations of alleged co-conspirators,
- III. The trial court erred in admitting into evidence Watkins' failure to file federal income tax returns for the three successive years immediately preceding the first year for which tax evasion was charged.

We hold that no error was committed by the trial court. Each alleged error will be discussed separately.

III.

Evidence of Theft.

The government must carry the burden

of proving an affirmative act of tax evasion to satisfy § 7201. Spies v. United States, 317 U.S. 492 (1943). See United States v. McNulty, 528 F.2d 1223 (9th Cir.), cert. denied, 425 U.S. 972 (1976). The government asserted at trial and argues here that certain evidence of theft was relevant to one of the affirmative acts charged. Appellant requested exclusion of the evidence on the ground that he had conceded the only fact to which the evidence was relevant and that the prejudicial impact of the evidence outweighed its probative value.

To understand the evidence to which appellant objects it is necessary to describe a provision of the federal income tax law. Section 631(a) of the Internal Revenue Code accords income from timber operations special treatment. It is a special elective provision that allows a taxpayer who meets the section's criteria to treat

the cutting of timber as the sale and exchange of a capital asset under section 1231.¹ The necessary criteria are: (1) the taxpayer must have owned or had a contract right to cut timber and sell it for his own account; (2) the taxpayer must have cut timber for sale on his own account; and (3) the taxpayer must have owned or held a contract right to the timber for more than six months before the beginning of the year. A taxpayer who cuts stolen timber fails to meet these criteria and cannot claim section 631(a) treatment, because he neither owns the timber nor has a contract right to cut or sell it in his own name.

It is undisputed that appellant harvested timber both in his own name and on behalf of other logging firms on a contractual basis. Through his accountant appellant presented the government with records of his timber business for 1973. Analysis thereof revealed that in 1973 ap-

pellant sold 1.4 million board feet of timber in excess of the amount he acquired through his logging operations. Again through his accountant appellant represented that the excess derived from cutting on a tract of land known as Sesech Gulch, which appellant had logged in his own behalf. The government theorized that instead the excess had been stolen by the appellant from the Ash Flat tract, which appellant had logged on behalf of another company. By falsely representing the source of the lumber, the government contended, Watkins sought to establish section 631 eligibility. Such conduct, the government concludes, constituted an affirmative act of tax evasion for purposes of § 7201.

At trial appellant's counsel repeatedly objected to the theft evidence. He stated that appellant did not dispute the volume figures presented by the government

as the amount of timber for which appellant was entitled to claim section 631(a) treatment. These figures excluded the 1.4 million board feet which the government claims had been stolen. Defense counsel therefore argued the evidences' only purpose -- to counter anticipated claims that the excess timber was harvested legally -- no longer existed. But this evidence also was relevant to the inference to be drawn from appellant's statement that the excess timber volume must have come from Sesech Gulch. The government sought by the evidence not merely to show a substantial tax due and owing, but also to show that Watkins provided, through his accountant, false information in an effort to avoid tax.

The admissibility of this evidence turns upon the interrelationship of four Federal Rules of Evidence. Fed. R. Evid. 401 defense "relevant evidence" as "evidence having any tendency to make the ex-

istence of any fact that is of consequence to the determination of the action more probable or less probable than it would be without the evidence." This standard is clearly met; the evidence tends to establish the required "affirmative act." See Edwards v. United States, 375 F.2d 862, 866 (9th Cir. 1967), overruled on other grounds, United States v. Bishop, 412 U.S. 346 (1973). Fed. R. Evid. 402, the second applicable Rule, provides that relevant evidence is admissible unless otherwise excludable. Fed. R. Evid. 404(b) permits evidence of other crimes, wrongs, or acts for a proper purpose, but prohibits the use of such evidence to prove a criminal disposition. See United States v. McDonald, 576 F.2d 1350 (9th Cir.), cert. denied, ___ U.S. __ & __, 99 S.Ct. 105 & 312 (1978). A proper purpose includes proof of a "plan" by which taxes were evaded. The evidence in question here

served that purpose thereby overcoming any bar of Rule 404(b). However, despite the relevance of the evidence, and the inapplicability of a specific exception to admissibility, Rule 403 gives a trial judge discretion to exclude the evidence. Rule 403 reads:

Although relevant, evidence may be excluded if its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury, or by considerations of undue delay, waste of time, or needless presentation of cumulative evidence.

The striking of the balance between the probative value of particular evidence and the danger of prejudice is unmistakably committed to the trial judge's discretion. United States v. Riggins, 539 F.2d 682, 683 (9th Cir. 1976), cert. denied, 429 U.S. 1045 (1977). See United States v. Curtis, 568 F.2d 643, 645-46 (9th Cir. 1978); United States v. Butcher, 557 F.2d 666, 670 (9th Cir. 1977). We defer to the trial

judge's assessment in the absence of a clear abuse of this discretion. We cannot say that admission of the theft evidence was a clear abuse of discretion. The judge carefully instructed the jury as to the limited purpose for which the evidence was admitted. Prejudice may have been generated, but the balance struck was within the bounds of the trial judge's discretion.

IV.

Co-Conspirator Testimony.

Appellant's argument that the trial judge erred in admitting testimony of alleged co-conspirators also fails. Appellant contends the government presented insufficient independent evidence connecting him to the alleged conspiracy. Such evidence is necessary under Fed. R. Evid. 801 (d) (2) (E) to exclude statements of co-conspirators from the definition of inadmissible hearsay. To establish the exclusion there must exist "independent proof of the

existence of the conspiracy and of the connection of the declarant and the defendant to it." United States v. Eubank, 591 F.2d 513, 519 (9th Cir. 1979); United States v. Weiner, 578 F.2d 757, 768 (9th Cir.), cert. denied, ___ U.S. ___, 99 S.Ct. 568 (1978); United States v. Snow, 521 F.2d 730, 733 (9th Cir. 1975), cert. denied, 423 U.S. 1090 (1976). The trial judge makes the initial determination whether a sufficient foundation has been established to make the declarations admissible. United States v. Eubank, supra, 591 F.2d at 519; United States v. King, 552 F.2d 833 (9th Cir. 1976), cert. denied, 430 U.S. 966 (1977). However, the trial judge may admit the challenged statements conditionally, subject to a later motion to strike if the prosecution fails to establish the required foundation. United States v. Eubank, supra, 591 F.2d at 519 n.6; United States v. Weiner, supra, 578 F.2d at 768. It is

not controlling, therefore, whether sufficient independent evidence connecting appellant with the conspiracy existed at the time the trial judge made his first ruling under Rule 801(d)(2)(E). The trial judge considered the sufficiency of the independent evidence before giving the case to the jury. Our review of the record convinces us that the government presented sufficient independent evidence of the "declarant's" and appellant's connection with a conspiracy to steal timber. We find no error in the admission of co-conspirator testimony.

V.

Prior Failure to File Returns.

The prosecuting attorney, in his opening statement, told the jury that appellant had not filed income tax returns "since 1958," and that "the evidence will show that Mr. Watkins not only did not file federal income tax returns, he did not file Oregon income tax returns either."

Subsequently the government did introduce evidence regarding the failure to file federal returns, but not state returns. The judge then struck testimony relating to appellant's failure to file federal returns prior to 1968. He instructed the jury to disregard the statements and evidence of the failure to file Oregon returns or federal returns other than after 1968 through 1971. In addition, the judge instructed the jury that the failure to file could be considered only as it bore upon appellant's intent.

Again, the relevant standard of review is "whether the district court abused its discretion when it decided that the tendency of the evidence in question to prove the essential elements of knowledge and intent outweighed its potential prejudice." United States v. Rocha, 553 F.2d 615, 616 (9th Cir. 1977). This court, in United States v. Snow, supra, 529 F.2d 224,

upheld the admission of evidence of failure to file income tax returns in similar circumstances.² Appellant attempts to distinguish Snow, arguing that in Snow the prosecution presumably was able to show that the defendant had a duty to file returns in those years for which evidence of a failure to file was admitted. But no such requirement is evident in Snow.

We hold, therefore, that the trial judge did not abuse his discretion in allowing the jury to consider the evidence of nonfiling for three years prior to the first year of the indictment. His estimate of the probability of undue prejudice is entitled to great weight. United States v. Pavon, 561 F.2d 799, 803 (9th Cir. 1977). In addition, his instruction to the jury that they should disregard any evidence concerning the defendant's alleged failure to file state income tax returns and any evidence concerning the defendant's failure

to file federal returns prior to 1968 eliminated any prejudice that may have stemmed from the prosecutor's opening statement. See United States v. Pavon, supra, 561 F.2d at 803.

AFFIRMED.

FOOTNOTES

1. Section 631 requires that a taxpayer make a binding election to employ its provisions on the return for the taxable year timber is cut. Such an election cannot be made on an amended return. Though it is arguable that Watkins may be precluded from the benefits of section 631(a) for civil purposes, the government conceded at trial that, for the purposes of a criminal case, Watkins would be allowed the benefits of that section as if he had made the requisite election in each year.

2. The defendant in Snow had been charged with filing false individual returns for 1968 through 1970 and failing to file an individual return for 1971. The trial judge admitted evidence that the defendant had failed to file a federal individual return for the six years preceding 1968. In addition, he admitted (Cont.)

2. (Cont.) evidence that the defendant had received notice of state tax liability in 1968. This court held that evidence of the defendant's failure to file federal and state income tax returns in pre-prosecution years was properly admissible as relevant to the issue of willfulness.

APPENDIX B
B-1

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

UNITED STATES OF AMERICA,)
Plaintiff-Appellee,) No. 78-2733
v.) ORDER
WALLACE W. WATKINS,)
Defendant-Appellant.)

Before: KILKENNY and SNEED, Circuit
Judges, and Waters*, District
Judge

The panel as constituted in the
above case has voted to deny the petition
for rehearing and to reject the suggestion
for rehearing en banc.

The full court has been advised of
the suggestion for en banc rehearing, and
no judge of the court has requested a vote
on the suggestion for rehearing en banc.

*Honorable Laughlin E. Waters, District
Judge for the Central District of California,
sitting by designation.

Fed. R. App. P. 35(b).

The petition for rehearing is denied and the suggestion for a rehearing en banc is rejected.

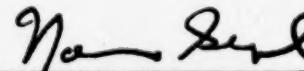
CERTIFICATE OF SERVICE

I hereby certify that I served the foregoing Petition for a Writ of Certiorari on the counsel for respondent by enclosing a copy thereof in an envelope, postage prepaid, addressed to:

The Hon. Wade H. McCree
Solicitor General of the
United States
Department of Justice
Washington, D.C. 20530

Mr. Ronald H. Hoevet
Asst. U.S. Attorney
P.O. Box 71
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Dated: August 14, 1979.



Norman Sepenuk
Attorney for Petitioner